IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

SECURITIES AND EXCHANGE COMMISSION, *Plaintiff*, v. CHRISTOPHER A. FAULKNER, et al *Defendants*.	§ § § § § § § § §	Case No. 3:16-cv-1735-D

NON-PARTY ROTHSTEIN KASS'S OPPOSITION TO THE *JINSUN* PLAINTIFFS' THIRD MOTION TO LIFT STAY, REQUEST FOR JUDICIAL NOTICE OF RECEIVER'S SETTLEMENT WITH ROTHSTEIN KASS, AND BRIEF IN SUPPORT

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[1] These entities are referred to collectively as "Rothstein Kass." Rothstein Kass previously appeared in this action through non-party Rothstein Kass & Company, PLLC ("Rothstein Kass PLLC"), the entity that was sued in the *Jinsun* Action. Rothstein Kass now includes Rothstein Kass P.A. d/b/a Rothstein Kass & Co. P.C. ("Rothstein Kass P.C.").

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I. INTRODUCTION

The *Jinsun* Plaintiffs'[2] Third Motion to Lift Stay (the "Motion") is both premature (in that it requests relief premised on a settlement agreement that the Court has not yet approved) and moot (in that it is superseded by the Receiver's recently filed motion to enter a bar order).[3] Both the Settlement Agreement and the Bar Order contain procedures for the *Jinsun* Plaintiffs to register their objections if they believe that their claims in the *Jinsun* Action should not be barred. These objection procedures are the only appropriate venue for the *Jinsun* Plaintiffs to raise—and the Court to adjudicate—arguments regarding their ability to bring claims in the *Jinsun* Action.

Given the pending motions to approve the Settlement Agreement and Bar Order, the *Jinsun* Plaintiffs' Motion should be denied under the applicable three-factor test identified in *SEC v. Wencke*, 742 F.2d 1230 (9th Cir. 1984) ("*Wencke*"). ***First***, the *Jinsun* Plaintiffs have not identified any injury that will result from continuing the Stay Order until, at the earliest, the Court has considered the Settlement Agreement and Bar Order. ***Second***, although the Receiver's lawsuit against Rothstein Kass is nearing an end, the Receiver needs the existing status quo to

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[2] The "*Jinsun* Plaintiffs" refers collectively to Jinsun, LLC, Silver Star Holdings Trust, TPH Holdings, LLC, Vertical Holdings, LLC, Steven Plumb, and J. Leonard Ivins, the Plaintiffs in *Jinsun, LLC et al. v. Rothstein Kass & Co.*, No. CC-17-06249-C (Cty. Ct. at Law No. 3, Dall. Cty., Tex.) ("*Jinsun* Action").

[3] *See* Receiver's Unopposed Motion to Approve Proposed Settlement with Rothstein Kass and Expedited Request for Entry of Scheduling Order and Brief in Support (Dkt. No. 591) (the "Settlement Motion") and Appendix in Support of Receiver's Unopposed Motion to Approve Settlement (Dkt. No. 592); Receiver's Motion to Enter Proposed Final Bar Order and Brief in Support (Dkt. No. 594) (the "Bar Order Motion") and Appendix in Support of Receiver's Motion to Enter Proposed Bar Order (Dkt. No. 595). The term "Settlement Agreement" refers to the settlement agreement between Rothstein Kass and the Receiver included at APP00004-14 of Dkt. No. 592. The term "Bar Order" refers to the [Proposed] Final Bar Order included at APP. 117-127 of Dkt. No. 595.

continue to finalize the settlement. If the Court lifts the stay for the *Jinsun* Action or does not enter the Bar Order, the Settlement Agreement will be rendered null and void. ***Third***, the *Jinsun* Plaintiffs' claims are ultimately meritless because they lack standing to bring any of their claims.

Because the *Jinsun* Plaintiffs lack standing to assert claims against Rothstein Kass, any objections raised by the *Jinsun* Plaintiffs to the Settlement Agreement or Bar Order will fail. All of the *Jinsun* Plaintiffs' remaining claims (and alleged injuries) in the *Jinsun* Action are derivative of claims held and injuries suffered by Receivership Entities[4] Bering Exploration, Inc. ("Bering") or Breitling Energy Corporation ("BECC"), if such claims exist at all. Because both Bering and BECC are Receivership Entities, the Receiver properly holds these claims. The Receiver therefore is well within his authority to settle such claims in the Settlement Agreement and to agree to entry of the Bar Order, which prohibits third parties from improperly bringing such claims against Rothstein Kass. In sum, the *Jinsun* Plaintiffs have alleged neither claims nor injuries independent of those possessed or suffered, respectively, by Receivership Entities. The *Jinsun* Plaintiffs' failure to articulate independent, non-derivative claims or damages—let alone both—renders their claims properly barred, and any discussion about whether the Stay Order[5] should be lifted as to the *Jinsun* Action is moot.

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[4] For ease of reference, Rothstein Kass uses the term "Receivership Entities" to refer to the entities that are under the Receiver's control, as the Court has done in prior orders. (*See, e.g.*, Dkt. No. 496 at 1.)

[5] "Stay Order" refers to the September 25, 2017, order appointing the Receiver in this action and staying all litigation involving receivership assets or receivership defendants. (*See* Dkt. No. 142.) The Court has since entered three amended orders appointing the Receiver. (*See* Dkt. Nos. 320, 418, 496.) These orders do not substantively modify the Stay Order language at issue here.

Rothstein Kass respectfully requests that this Court deny the Motion and allow the Stay Order to remain in force at least until the Court rules on the pending motions relating to the Settlement Agreement and Bar Order.

II. RELEVANT FACTUAL BACKGROUND AND PROCEDURAL HISTORY

This Court has addressed the Stay Order's application to the *Jinsun* Action several times. (*See* Dkt. Nos. 332, 408, 512, 527, 550.) Each time, this Court has recognized that the litigation stay in this case applies to the *Jinsun* Action. (*See id.*) Nevertheless, certain key facts and events in the procedural history bear repeating.

A. Relevant Factual Background

The *Jinsun* Plaintiffs' allegations against Rothstein Kass in the *Jinsun* Action all stem from a reverse merger between Bering, a public corporation, and Breitling Oil and Gas Corporation ("BOG") and Breitling Royalties Corporation ("BRC") (together, "Breitling") on December 9, 2013 (the "Reverse Merger"). Through the Reverse Merger, Bering acquired Breitling's assets in exchange for approximately 92.5% of Bering's issued shares. (App. at 138, Ex. D.) Bering survived this transaction and soon thereafter changed its name to Breitling Energy Corporation ("BECC"). Because BECC and Bering are the same company by different names, Bering is a Receivership Entity. (*See* Dkt. No. 512 at 11 ("Bering, however, became the receivership defendant BECC. The Receiver is entitled to pursue, and has, in fact, pursued, claims for damages both to Bering (pre-merger) and to BECC (post-merger).").) The *Jinsun* Plaintiffs were not parties to the agreement that effectuated the Reverse Merger (the "Asset Purchase Agreement"). (App. at 43, Ex. B.)

Breitling, and, after the Reverse Merger, BECC, hired Rothstein Kass to audit financial statements prepared by Breitling and BECC. (App. at 268-83, Exs. H, I.) Rothstein Kass

provided its audit opinion for Breitling's financial statements for the two-year period ended December 31, 2011 and December 31, 2012 on February 14, 2014—several months after the Reverse Merger closed. (App. at 133, Ex. D.) Rothstein Kass later provided its audit opinion for BECC's financial statements for the period ended December 31, 2013 on March 31, 2014—again, several months after the Reverse Merger closed. (App. at 221, Ex. E.) The *Jinsun* Plaintiffs have conceded that Rothstein Kass's alleged misrepresentations and omissions occurred in its audit opinions and that Rothstein Kass did not have any separate communications with the *Jinsun* Plaintiffs. (App. at 264, Ex. G.)[6]

In sum, the *Jinsun* Plaintiffs blame Rothstein Kass's audits for *Bering's* entry into the Reverse Merger. The *Jinsun* Plaintiffs' pleadings and expert disclosures make clear that their claims and alleged damages are based entirely on this event:

- "If Rothstein Kass had not issued an unqualified audit opinion, the reverse merger transaction would have failed, Breitling would never have become a publicly traded company, and ***Plaintiffs would have been able to keep their stock in Bering as well as all of its valuable assets***." (App. at 8-9, Ex. A (emphasis added).)

- ". . . [The *Jinsun*] Plaintiffs would not have allowed Bering to go forward with the transaction, [the *Jinsun*] Plaintiffs would still own their shares in Bering, and [the *Jinsun*] Plaintiffs could have either continued operating Bering as a public company or they could have otherwise sold it to another company . . . ." (Dkt. No. 587 at 8.)

- "Plaintiffs have been damaged (i) by the failure to realize the full potential of Bering's combined proved and probable oil and gas assets and (ii) the loss of value of the BECC shares received through the Transaction resulting from their reliance on Breitling/BECC's fraudulent financial statements." (App. at 96, Ex. C.)

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[6] Vertical Holdings, LLC's responses to the First Set of RFAs in the *Jinsun* Actions are included as an example. (*See* App., Ex. G.) Every other *Jinsun* Plaintiff also admitted that they did not communicate with Rothstein Kass.

The facts and the *Jinsun* Plaintiffs' admissions undermine *any* contention that their claims are independent of claims owned by the Receiver or that the *Jinsun* Plaintiffs suffered any alleged injury separate from the entities in which they owned stock (*i.e.*, Bering and BECC). As noted above: (i) Rothstein Kass never audited Bering, (ii) Rothstein Kass never communicated with Bering or the *Jinsun* Plaintiffs, and (iii) Bering closed on the Reverse Merger over two months *before* Rothstein Kass issued its first audit opinion.

B. Relevant Procedural History

On June 24, 2016, the U.S. Securities & Exchange Commission ("SEC") filed suit against several of the Receivership Entities and several related officers and employees of the Receivership Entities, including BECC's CEO, Christopher Faulkner (the "SEC Action"). On August 14, 2017, the Court appointed Thomas L. Taylor III as temporary Receiver over Defendants Faulkner's, BOG's, and BECC's oil-and- gas-related assets. (*See* Dkt. No. 108.) On September 25, 2017, the Court expanded the Receiver's scope by entering the Stay Order, which enjoined the continuation or commencement of all "Ancillary Proceedings" involving, among other things, Receivership Assets or current or former officers, directors, and agents of the Receivership Entities. (*See* Dkt. No. 142.)

The Stay Order defines "Receivership Assets," to include "all assets—in any form or of any kind whatsoever— owned, controlled, managed, or possessed by…, directly or indirectly," the Receivership Entities. (Dkt. No. 142 at 1.) The Receiver is empowered to investigate and prosecute claims "in his discretion" to recover funds for the receivership estate. (*Id.*, ¶¶ 42-43.)

Notwithstanding the terms of the Stay Order, the *Jinsun* Plaintiffs—shareholders and former officers and directors of Bering—sued Rothstein Kass & Co., PLLC[7] in state court on November 28, 2017, for various claims related to Rothstein Kass's audits of Breitling and BECC. Less than a year later, on October 24, 2018, this Court issued a Memorandum Opinion and Order clarifying that the Stay Order applied to the *Jinsun* Action because equitable and disgorgement claims in that action belonged to the Receiver and two of the *Jinsun* Plaintiffs brought the suit as former officers and directors of Bering. (*See* Dkt. No. 332.) On December 13, 2018, the *Jinsun* Plaintiffs sought to vacate that order. The Court denied the motion. (*See* Dkt. No. 408.) Without further approval from this Court, the *Jinsun* Plaintiffs continued to litigate in state court.

After additional discovery and amendments to the *Jinsun* Plaintiffs' pleadings demonstrated that the *Jinsun* Plaintiffs' claims and alleged injuries were derivative of claims and alleged injuries of Receivership Entities Bering and BECC, Rothstein Kass filed a further motion to clarify the Stay Order on October 16, 2019. (*See* Dkt. No. 487.) On February 6, 2020, this Court issued its Memorandum Opinion and Order concluding that the *Jinsun* Action continued to be stayed because additional claims brought by the *Jinsun* Plaintiffs (*i.e.*, aiding and abetting breach of fiduciary duty and conspiracy to aid and abet a breach of fiduciary duty) were assets of the Receiver and the *Jinsun* Action impacts the "potential rights or property of the receivership estate." (*See* Dkt. No. 512.)

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[7] The *Jinsun* Plaintiffs have since stated that Rothstein Kass P.A. is the proper defendant. For ease of reference, Rothstein Kass will be referred to collectively in discussing the suits and the Rothstein Kass entities.

On February 10, 2020 the *Jinsun* Plaintiffs filed an "emergency" motion to lift the Stay Order, offering to non-suit the aiding and abetting breach of fiduciary duty and conspiracy to aid and abet breach of fiduciary duty claims. (*See* Dkt. No. 516.) Rothstein Kass opposed this motion, explaining that the *Jinsun* Plaintiffs' remaining claims and alleged injuries are all derivative of claims owned by the Receiver and injuries purportedly suffered by Receivership Entities. (*See* Dkt. No. 521 at 10-17.) This Court denied the *Jinsun* Plaintiffs' motion, holding that the Stay Order continued to apply to the *Jinsun* Action even if the *Jinsun* Plaintiffs nonsuited the aiding and abetting breach of fiduciary duty and conspiracy to aid and abet breach of fiduciary duty claims. (*See* Dkt. No. 527.) A few months later, on July 1, 2020, the Court denied another motion to lift the Stay Order brought by the *Jinsun* Plaintiffs to correct the name of the defendant in the *Jinsun* Action. (*See* Dkt. No. 550.)

During the pendency of the *Jinsun* Action, the Receiver has been litigating his claims against Rothstein Kass and Brian Matlock since he filed his complaint on July 1, 2019. Following this Court's order granting in part and denying in part Rothstein Kass's motion to dismiss, the Receiver filed an Amended Complaint on April 24, 2020 asserting claims for negligence and participation in breaches of fiduciary duties. (*Taylor v. Rothstein Kass, et al.*, No. 3:19-cv-1594-D (N.D. Tex.) (the "*Receiver* Action"), Dkt. No. 45.) The Receiver and Rothstein Kass have now agreed to settle the Receiver's remaining claims, as detailed in the Receiver's Settlement Motion. (Dkt. No. 591, ¶¶ 15-23.) The Settlement Agreement is conditioned on this Court's entering a related Bar Order. (*See, e.g.*, Dkt. No. 591 at 5 n.3, 12; Dkt. No. 592 at APP00006-7 ("The Agreement is conditioned on the Receivership Court granting the Receiver's Bar Order Motion and entering the Bar Order and upholding the Bar Order in response to any objections or challenges . . . .").)

Prior to the Receiver's filing the Settlement Motion, the *Jinsun* Plaintiffs filed the instant Motion seeking to lift the Stay Order so that they may pursue their remaining claims of "aiding and abetting violations of the Texas Securities Act, negligent misrepresentation, and fraud." (*See* Dkt. No. 587; Dkt. No. 523 at 4.)

III. ARGUMENT

A. Lifting The Stay Is Not Warranted Under *Wencke*

A close examination of the *Wencke* test further demonstrates that the Motion should be denied. As this Court previously observed, the *Wencke* test has three factors: "(1) whether refusing to lift the stay genuinely preserves the status quo or whether the moving party will suffer substantial injury if it is not permitted to proceed; (2) the time in the course of the receivership at which the motion for relief from the stay is made; and (3) the merits of the moving party's underlying claim." (Dkt. No. 527 at 4 (citing *SEC v. Stanford Int'l Bank Ltd*., 424 Fed. Appx. 338, 341 (5th Cir. 2011) (per curiam)).)

1. Preserving the Status Quo Outweighs the Jinsun Plaintiffs' Interests

This Court previously noted that the first *Wencke* factor is "essentially a balancing of the *Jinsun* Plaintiffs' interests with the interests of the receivership." (Dkt. No. 527 at 6 (citing *Stanford*, 424 Fed. Appx. At 341).) The *Jinsun* Plaintiffs fail to identify any injury that they will suffer if the Stay Order continues in effect until the Court can consider the Settlement Agreement and Bar Order. Previously, the *Jinsun* Plaintiffs have argued that one of the *Jinsun* Plaintiffs, Mr. Ivins, would suffer injury from the Stay Order because he is elderly and in ill-health and thus may not be able to complete the *Jinsun* Action if it is delayed. (*See* Dkt. No. 516 at 4-5.) Although Rothstein Kass remains sympathetic to Mr. Ivins' circumstances, his declining health does not outweigh the interests of the Receiver—and the thousands of claimants in the

receivership estate—in finalizing the Settlement Agreement and Bar Order. Rothstein Kass's settlement with the Receiver is conditioned on this Court's entry of the Bar Order, which would preclude the *Jinsun* case from proceeding. (*See, e.g.*, Dkt. No. 592 at APP00007 (". . . if the Receivership Court does not enter or uphold the Bar Order, the Agreement shall be considered null and void."). If the Court lifts the Stay Order now and lets the *Jinsun* Action proceed, the Settlement Agreement would no longer be valid.

In contrast, any harm to the *Jinsun* Plaintiffs (assuming *arguendo* that their objections to the Settlement Agreement and Bar Order were even successful, which is unlikely) would be limited to the few months required to resolve their objections. (*See* Dkt. No. 592 at APP00019 ("Any Person who wishes to object to the terms of the Agreement, or to the Bar Order Motion, must do so . . . no later than [61 days after entry of this Scheduling Order]."").) A potential delay of a few months for three individuals to pursue their claims cannot outweigh the interests of thousands of claimants in maximizing their recovery from the receivership estate. *See US v. Acorn Tech. Fund LP*, 429 F.3d 438, 449 (3d Cir. 2005) ("Not being allowed the first bite at the apple is not the kind of substantial injury we will recognize under the first prong of *Wencke*.").

2. The Court Should Rule on the Receiver's Pending Motions Related to the Settlement Agreement and Bar Order Before Addressing the Stay Order

The second *Wencke* factor also weighs against granting the Motion. The *Jinsun* Plaintiffs appear to argue that the Stay Order is no longer necessary for the Receiver because the Receiver and Rothstein Kass have entered into a preliminary settlement. (*See* Dkt. No. 587 at 1.) The settlement, however, is not final. Indeed, as noted above, an order barring the *Jinsun* Plaintiffs' claims in the *Jinsun* Action is a condition of the Settlement Agreement, and the *Jinsun* Plaintiffs have an opportunity to object to the Settlement Agreement and Bar Order. (*See* Dkt. No. 591 at

12, 21; Dkt. No. 594 at 2-3, 18.) Thus, it is not appropriate to lift the Stay Order while motions are pending regarding approval of the Settlement Agreement and Entry of the Bar Order. *See, e.g.*, *Acorn Tech.*, 429 F.3d at 449-50 (second *Wencke* factor weighs against lifting stay even though the receivership has been in place "for 30-36 months"); *SEC v. Universal Financial*, 760 F.2d 1034, 1038-39 (9th Cir.) (second *Wencke* factor weighs against lifting stay even though the receivership has been in place "almost four years").

The court's reasoning in *SEC v. Illarramendi*, No. 3:11cv78 (JBA), 2012 WL 5832330, at *2-3 (D. Conn. Nov. 16, 2012) is particularly instructive. In *Illarramendi*, intervenors in an SEC enforcement action sought an order lifting the stay of related litigation to pursue a claim against the receiver in a foreign court while the court was weighing objections to a settlement agreement. *Illarramendi*, 2012 WL 5832330 at *1-2. The intervenors in *Illarramendi*, just like the *Jinsun* Plaintiffs, (i) failed to articulate any reason to lift the litigation stay under the applicable *Wencke* factors and (ii) had access to alternative procedures for pursuing their claims, including objecting to a pending settlement or participating in the receivership's claims process. *Id.* at *1-3. The court in *Illarramendi* focused on these facts, criticizing the movants for "fail[ing] to show how they will 'suffer substantial injury if not permitted to proceed' against the Receiver in the manner they prefer, rather than in the context of the claims process." *Id.* at *2. Ultimately, the court in *Illarramendi* denied the intervenors' request because they "have failed to identify why, under *Wencke*, the anti-litigation stay should be lifted as to them." *Id.* at *3. The reasoning in *Illarramendi* applies with equal force to the *Jinsun* Plaintiffs' Motion.

3. The *Jinsun* Plaintiffs Lack Standing to Bring Any Claim Asserted in the *Jinsun* Action

Finally, the third *Wencke* factor weighs against granting the Motion. The *Jinsun* Plaintiffs did not attempt to defend the merits of their claims. Nevertheless, it is clear that all of

these claims are meritless because they are derivative of claims properly held by Bering and BECC and, through them, the Receiver. *See Acorn Tech.*, 429 F.3d 438, 445 (3d Cir. 2005) ("[W]e agree that [the movants'] . . . mismanagement claims can only be brought derivatively and therefore also fail as a matter of law.").

This Court has previously applied the two-part test in *SEC v. Sharp Capital, Inc.*, 315 F. 3d 541 (5th Cir. 2003) (upholding permanent injunctions barring investors from pursuing claims against third parties in state court following settlement between third parties and court-appointed special master) to determine whether claims asserted by the *Jinsun* Plaintiffs are derivative and properly belong to the Receiver:

> To determine whether a given claim belongs to the receivership estate, it is appropriate to conduct a Fed. R. Civ. P. 12(b)(6)-type analysis, looking only at the allegations in the complaint. *See SEC v. Sharp Capital, Inc.*, 315 F.3d 541, 544 (5th Cir. 2003). The Fifth Circuit has endorsed (in *dicta*) a two-part test: if (1) the cause of action alleges only an indirect harm to the plaintiff—one that derives from harm to a receivership entity—and (2) a receivership entity could have itself raised the claim for its own direct injury, then the claim belongs to the Receiver. *See id.* (quoting *In re Educators Grp. Health Tr.*, 25 F.3d 1281, 1284 (5th Cir. 1994)).

(Dkt. No. 408 at 7; *see also* Dkt. No. 512 at 6.) *See also In re Seven Seas Petroleum, Inc.*, 522 F.3d 575, 584 (5th Cir. 2008) ("Whether a particular state-law claim belongs to the [receivership] estate depends on whether under applicable state law the [receivership entity] could have raised the claim as of the commencement of the case. As part of this inquiry, we look to the nature of the injury for which relief is sought and consider the relationship between the [receivership entity] and the injury.") (citations omitted). All of the *Jinsun* Plaintiffs' remaining claims (*i.e.*, fraud, negligent misrepresentation, and aiding and abetting a breach of the Texas Securities Act) in the *Jinsun* Action are property of the Receiver under the *Sharp Capital* Test.

a. The *Jinsun* Plaintiffs' Claims Are Derivative Because They Allege Only Indirect Injuries

Nothing material has changed concerning the *Jinsun* Plaintiffs' pleading theory since February 2020, when the Court concluded the stay applied to the *Jinsun* Action notwithstanding the *Jinsun* Plaintiffs' agreement to dismiss their claims for aiding and abetting breach of fiduciary duty and participating in a conspiracy to breach fiduciary duty. (*See* Dkt. No. 527 at 3, 6.) The *Jinsun* Plaintiffs continue to allege that but for Rothstein Kass's actions they would (somehow) have been able to unwind the Reverse Merger—which closed months before Rothstein Kass issued any audit opinion on Breitling's financial statements—and everything would have returned to the pre-Reverse Merger *status quo ante*.[8] (*See, e.g.*, Dkt. No. 587 at 8 ("Had Rothstein Kass blown the whistle on Breitling . . . [we] would not have allowed Bering to go forward with the transaction, [we] would still own [our] shares in Bering, and [we] could have either continued operating Bering as a public company or [we] could have otherwise sold it to another company . . . .").) But only Bering's officers and directors could have controlled its entry into the Reverse Merger, continued operations, or sale to another company. In other words, the *Jinsun* Plaintiffs not only continue to allege injuries stemming from a transaction (the Reverse Merger) to which they were not parties and which affected all shareholders of Bering equally on the basis of the shares owned, but base their pleading theory on their ability as *officers and directors of Bering* to stop a Receivership Entity from entering into the Reverse Merger with two other Receivership Entities.[9]

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[8] The *Jinsun* Plaintiffs conveniently neglect to mention that the *status quo ante* involved a worthless company that was walking its "final mile" prior to the Reverse Merger. (*See* App. at 285, Ex. J; *id.* at 292-94, Ex. K.)

[9] Of course, the Court has already held that the Stay Order applied to the *Jinsun* Plaintiffs' claims to the extent they were brought on behalf of Bering's officers and directors. (*See* Dkt. No. 332 at 9.) Indeed, the *Jinsun* Plaintiffs' theory articulated in their Motion appears to

Specifically, the *Jinsun* Plaintiffs offer two damages theories: (i) they complain about a loss of value to their Bering/BECC shares,[10] and (ii) they claim a right to recover assets previously belonging to Bering.[11] Indeed, they have alleged in their operative petition that:

> If Rothstein Kass had not issued an unqualified audit opinion, the reverse merger transaction would have failed, Breitling never would have become a publicly traded company, and Plaintiffs would have been able to keep their stock in Bering as well as all of its valuable assets.

(See App. at 9, Ex. A; s*ee also* App. at 17 (". . . without an unqualified audit opinion—Bering would still be a publicly traded company and Plaintiffs would still own Bering's assets") and at 33-34 (". . . Plaintiffs have suffered actual damages in the lost value of their shares. . .").) In

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contradict their previous assurances to the Court that they are not bringing claims as officers and directors of Bering. (*See* Dkt. No. 358 at 1 ("[A] Sixth Amended Petition, if allowed to be filed, establishes that the claims of Leonard Ivins and Steven Plumb are brought solely in their capacities as former shareholders of Bering Exploration, Inc. and the prosecution of these claims have nothing to do with the fact that Ivins and Plumb were former officers and/or directors of Breitling").)

[10] Although the *Jinsun* Plaintiffs previously claimed they were seeking damages as a result of a diminution in the value of their shares in BECC, they have since seemingly changed their claims and now state they are seeking damages relating to their shares in Bering. (*Compare* App. at 96, Ex. C *with* Dkt. No. 587 at 8.) As this Court has already observed, Bering and BECC are merely different names for the same company, which is a Receivership Entity either way, so it makes no difference whether the *Jinsun* Plaintiffs claim diminution in the value of their shares of Bering or BECC.

[11] The specific Bering asset is, presumably, the North Edna oil and gas well, which the *Jinsun* Plaintiffs explicitly admitted belonged to Bering. (*See, e.g.*, App. at 241, Ex. F ("Plaintiffs' former company, Bering . . ., owned the North Edna oil and gas lease rights on an uninterrupted basis until those ownership rights were conveyed to [Breitling] in the very reverse merger transaction that was procured by fraud, which created this litigation."), 246 ("The North Edna oil and gas lease remained an asset of Bering [] on an uninterrupted basis through the closing date in December of 2013 with Breitling."), 254 ("Bering Exploration never modified its ownership rights in the North Edna Oil and Gas Lease—*until Bering Exploration conveyed those rights to Breitling in the merger*."), 256-57 ("Bering Exploration owned the [North Edna] lease. . . Because Plaintiffs' former company, Bering Exploration, lost the North Edna Oil and Gas Lease in the merger transaction which was predicated on fraud that the Defendant was well-aware, it is a proper component of Plaintiffs' damages' [sic] claim").)

sum, the *Jinsun* Plaintiffs allege injuries both as Bering's shareholders (for the lost value of shares in Bering/BECC) and on behalf of Bering itself (for the lost value of Bering's purportedly valuable assets).

This Court has already recognized that any damages resulting from claims based on the *Jinsun* Plaintiffs' status as shareholders grants them no "separate and independent right of action for injuries suffered by the corporation which merely result in the depreciation of the value of their stock." (Dkt. No. 512 at 11 (citing *Wingate v. Hajdik*, 795 S.W.2d 717, 719 (Tex. 1990)); *see also id.* ("Thus to recover for wrongs done to the corporation, the shareholder must bring the suit derivatively in the name of the corporation so that each shareholder will be made whole if the corporation obtains compensation from the wrongdoer.") (citing *Webre v. Sneed*, 358 S.W.3d 322, 329-30 (Tex. App.—Houston [1st Dist.] 2011), *aff'd*, 465 S.W.3d 169 (Tex. 2015)).)

Accordingly, the *Jinsun* Plaintiffs lack standing to pursue their remaining claims for fraud, negligent misrepresentation, and aiding and abetting a violation of the Texas Securities Act; such claims must be brought, if at all, in the name of the corporation.[12] *Stevens v. Lowder*,

[12] The *Jinsun* Plaintiffs previously argued in separate briefing that Rothstein Kass has somehow waived its opportunity to raise with this Court the *Jinsun* Plaintiffs' lack of standing for their asserted claims. (*See* Dkt. No. 523 at 2-3, 9.) This argument is unavailing. There is no reason—and the *Jinsun* Plaintiffs provide none—why procedural pleading rules in state court would prevent this Court's from analyzing whether a particular legal claim is an asset of the Receiver. Furthermore, the Jinsun Plaintiffs conflate "standing" and "capacity." The relevant inquiry here is whether the *Jinsun* Plaintiffs have *standing* to assert their claims, not *capacity*, and both parties are well aware of this issue, having actively litigated it for several years. *See County of El Paso v. Navar*, 584 S.W.3d 73 (Tex. App.—El Paso 2018) ("A plaintiff has standing to bring a lawsuit when it is personally aggrieved, regardless of whether it is acting with legal authority; a plaintiff has capacity when it has the legal authority to act, regardless of whether it has a justiciable interest in the controversy."); *Basic Capital Management v. Dynex Commercial, Inc.*, 348 S.W.3d 894, 989-99 (Tex. 2011) ("Regardless of whether the issue is properly denominated standing, as the parties seemed to think in the trial court, or capacity, as petitioners have argued on appeal, the *substance* of Dynex's assertion—that ART and TCI cannot recover for Dynex's breaches of its agreements because they were not parties to the agreements—was addressed in cross-motions for summary judgment and adjudicated prior to trial.") (emphasis in original).

643 F.2d 1078, 1080 (5th Cir. 1981); *see also Abdu v. Hailu*, No. 05-17-01261-CV, 2018 WL 6716547, at *2 (Tex. App. —Dallas Dec. 21, 2018) ("A corporate shareholder lacks standing to sue in her own name or for her own benefit on a cause of action belonging to the corporation, even if the shareholder is indirectly injured through injury to the corporation."); *Ritchie v Rupe*, 443 S.W.3d 856, 887-88 (Tex. 2014) ("[I]ndividual stockholders have no separate and independent right of action for injuries suffered by the corporation which merely result in the depreciation of the value of their stock.") (quoting *Mass v. Davis*, 140 Tex. 398, 407 (1942)); *Kauffman v. Dreyfus Fund, Inc.*, 434 F.2d 727, 732 (3d Cir. 1970) ("A stockholder of a corporation does not acquire standing to maintain an action in his own right . . . [when] the only injury to the shareholder is the indirect harm which consists in the diminution in value of his corporate shares resulting from the impairment of corporate assets."), *cert. denied*, 401 U.S. 974, 91 S.Ct. 1190, 28 L.Ed.2d 323 (1971).

Nor can the *Jinsun* Plaintiffs assert any claim on behalf of Bering for the alleged diminution in value of Bering's assets. "An individual shareholder, by virtue of his ownership of shares, does not own the corporation's assets . . . ." *Collins v. Mnuchin*, 938 F.3d 553, 624 (5th Cir. 2019) (quoting *Dole Food Co. v. Patrickson*, 538 U.S. 468, 474-75 123 S.Ct. 1655 (2003)). The *Jinsun Plaintiffs*' damages expert recognized that the *Jinsun* Plaintiffs are trying to recover their proportionate share of the value of Bering's assets by reducing the *Jinsun* Plaintiffs'

Although the *Jinsun* Plaintiffs have not raised this argument in their Motion, Rothstein Kass preemptively addresses it here in case the *Jinsun* Plaintiffs improperly raise it for the first time in their forthcoming reply (as they did in their motion for emergency relief). (*See* Dkt. No. 527 at 3 n.5 ("To the extent [the *Jinsun* Plaintinffs] have attempted to remedy this deficiency by expanding on the reasoning in their reply brief . . . the [C]ourt declines to consider the expanded reasoning found in the reply brief.").)

purported damages related to North Edna to their percentage ownership of BECC's total shares. (App. at 98, Ex. C.)

The *Jinsun* Plaintiffs cannot escape this limitation by arguing that Bering is not a Receivership Entity. (*See, e.g.*, Dkt. No. 587 at 10 ("[The] Receiver has not, did not, and could not assert [our] individualized claims, the genesis of which derive from [our] ownership interests and shares in *Bering* long *before* the merger with Faulkner . . . .") (emphasis in original).) The Court has already rejected this argument. (*See* Dkt. No. 512 at 11 ("First, the *Jinsun* Plaintiffs assert that Bering is "not []part of the receivership." Bering, however, became the receivership defendant BECC. The Receiver is entitled to pursue, and has, in fact, pursued, claims for damages both to Bering (pre-merger) and to BECC (post-merger).") (citations omitted).)

b. Bering or BECC—and Therefore the Receiver—Could Have Raised All of the *Jinsun* Plaintiffs' Remaining Claims

Setting aside the merits of the Receiver's potential claims against Rothstein Kass and Rothstein Kass's affirmative defenses to such claims, the *Jinsun* Plaintiffs' claims belong to the Receiver and the Receiver has (or could have) brought any of the remaining claims alleged by the *Jinsun* Plaintiffs: fraud, negligent misrepresentation, and aiding and abetting a violation of the Texas Securities Act.

This Court's prior analysis in its March 5, 2019 and February 6, 2020 Orders is instructive for analyzing the *Jinsun* Plaintiffs' remaining claims. (*See* Dkt. No. 408 at 9-10; Dkt. No. 512 at 9.) In the March 5, 2019 Order, the Court discussed the *Jinsun* Plaintiffs' professional negligence claim, which has since been non-suited. The Court noted that the *Jinsun* Plaintiffs' core allegation was that "they would have rescinded the reverse merger transaction but for Rothstein Kass's acts and omissions. Had they done so, BECC would never have fallen into

Faulkner's hands, and the scale of the overall fraud scheme—and its resulting harm to a number of receivership entities—would have been reduced." (Dkt No. 408 at 10.) Accordingly, the "Receiver may bring a professional negligence suit on behalf of these entities" and the *Jinsun* Plaintiffs' "claim for professional negligence is necessarily derivative of the potential claims of a receivership entity." (*Id.* at 9-10; *see also id.* at 9 (citing *Haut v. Green Café Mgmt., Inc.*, 376 S.W.3d 171, 177 (Tex. App.—Houston [14th Dist.] 2012, no pet.) and *Wingate*, 795 S.W.2d at 719 for the proposition that "[t]he general rule in Texas is that a corporate shareholder has no individual cause of action for damages caused by a wrong done solely to the corporation.")

Similarly, in the February 6, 2020 Order, the Court analyzed the *Jinsun* Plaintiffs' claims that Rothstein Kass aided and abetted, or participated in a conspiracy to aid or abet, fiduciary duties purportedly owed to the *Jinsun* Plaintiffs. (Dkt. No. 512 at 9.) The Court again reached the same conclusion: "the harm to the *Jinsun* Plaintiffs is an indirect harm . . . because the duty arose, if at all, between Breitling's management and officers, on the one hand, an Bering (which is now BECC), on the other hand." *Id.*

c. The Receiver Already Brought Claims Sounding in Fraud and Negligence Against Rothstein Kass

Although the claims at issue have changed, the essence of the *Jinsun* Plaintiffs' allegations has not. For example, the *Jinsun* Plaintiffs' fraud-based and negligent misrepresentation claims are still based on the same premise: but for Rothstein Kass's alleged failure to disclose information it supposedly learned during its audits of *Breitling*, *Bering* would not have entered into the Asset Purchase Agreement, it would not have become a public company, and the Reverse Merger would (somehow) have been unwound. However, the *Jinsun* Plaintiffs' admission that Rothstein Kass *never* communicated with them precludes any independent claim they could have for fraud or negligent misrepresentation. (App. at 264,

Ex. G.) Put simply, there is no actionable representation to the *Jinsun* Plaintiffs to support any of these claims, all of which are derivative of claims belonging to the Receiver.

Even the *Jinsun* Plaintiffs' claim for fraud by nondisclosure is derivative of a claim properly asserted (if at all) by Bering or BECC. It is undisputed that Rothstein Kass's only clients were Breitling and later BECC. Rothstein Kass therefore had no contractual, fiduciary, or confidential relationship with the *Jinsun* Plaintiffs themselves (or even with Bering prior to the Reverse Merger). A fraud by non-disclosure claim requires a duty to disclose, which typically does not exist absent evidence of a confidential or fiduciary relationship. *Bombardier Aerospace Corp. v. SPEP Aircraft Holdings, LLC*, 572 S.W.3d 213, 219–20 (Tex. 2019). Although a party may have a "duty to speak" in limited circumstances, *see White v. Zhou Pei*, 452 S.W.3d 527, 537-38 (Tex. App.—Houston [14th Dist.] 2014), the *Jinsun* Plaintiffs' admissions that Rothstein Kass did not communicate with them prior to the Reverse Merger eliminated any possibility that such a duty could have arisen and caused their alleged damages. (*See* App. at 264, Ex. G.)

While the *Jinsun* Plaintiffs have no independent basis to pursue fraud and negligence claims against Rothstein Kass, the Receiver has already brought similar claims relating to Rothstein Kass's audit opinions. Alleging many of the same facts alleged by the *Jinsun* Plaintiffs regarding Rothstein Kass's audit of the Breitling Audit Entities, the Receiver's original complaint alleged that Rothstein Kass was negligent in the performance of the audit (Count I) and aided and abetted or participated in BECC's fraudulent scheme (Count III). (*See Receiver* Action (Dkt. No. 1), ¶¶ 82-83, 88-89.) Although the Court dismissed the Receiver's causes of action grounded in fraud on the basis that these claims are not clearly cognizable under Texas law and were not pleaded with particularity (*Receiver* Action (Dkt. No. 34) at 19-20), that is of no matter to the present inquiry before the Court, which turns on standing. (*See* Dkt. No. 408 at

7 ("That the defendant may have a valid defense on the merits of a claim brought by the [receivership entity] goes to the resolution of the claim, and not to the ability of the [receivership entity] to assert the claim.") (quoting *In re Educators*, 25 F.3d at 1286.).)

d. The Receiver Is the Only Plaintiff Who Could Bring a Claim for Aiding and Abetting a Violation of the Texas Securities Act Arising from the Reverse Merger

The *Jinsun* Plaintiffs also allege that Rothstein Kass aided and abetted Breitling/BECC and its officers, directors, and managers to violate the Texas Securities Act, Art. 581-33(A)(2), in connection with the Reverse Merger. Texas Securities Act, Art. 581-33(A)(2), in relevant part, provides:

> Untruth or Omission. ***A person who offers or sells a security*** (whether or not the security or transaction is exempt under Section 5 or 6 of this Act) by means of an untrue statement of a material fact or an omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading***, is liable to the person buying the security from him***, who may sue either at law or in equity for rescission, or for damages if the buyer no longer owns the security.

Emphasis added.

As discussed previously, *see* Section II.A. *supra*, the Reverse Merger involved an exchange of Bering's shares for Breitling's assets. (*See* App. at 42, Ex. B.) The *Jinsun* Plaintiffs were not parties to the Asset Purchase Agreement, and did not buy, sell or offer to sell any of their Bering shares in the Reverse Merger. (*See id.*) As a result, they lack standing under the Texas Securities Act to sue the person who offered or sold securities in the Reverse Merger. *Ratner v. Sioux Nat. Gas Corp.*, 770 F.2d 512, 517 (5th Cir. 1985).[13] Although the Receiver did

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[13] Ironically, the only party who could be liable for a primary violation of the Texas Securities Act cited by the *Jinsun* Plaintiffs is Bering. The party liable for a violation under the Act is the party that *sells* securities. The only party that sold securities in the Reverse Merger was

not assert a claim against Rothstein Kass for aiding and abetting a violation of the Texas Securities Act, he is the only plaintiff who could do so (assuming *arguendo* that such a claim exists). Each and every party to the Asset Purchase Agreement that consummated the Reverse Merger—BOG, BRC, and Bering—is now a Receivership Entity. As such, whether BOG, BRC, or Bering suffered a legally cognizable injury as a result of the "offer or sale of a security" in the Reverse Merger, the Receiver is the only plaintiff who could bring such a claim.

e. Recent Fifth Circuit Decisions in *Zacarias* and *Rotstain* Confirm That the *Jinsun* Plaintiffs Should Not Be Allowed to Pursue Their Claims Against Rothstein Kass Because Their Claims Are Derivative of the Receiver's Claims

The Fifth Circuit's recent holdings in *Zacarias v. Stanford Int'l Bank, Ltd.*, 945 F.3d 883 (5th Cir. 2019) ("*Zacarias*") and *Rotstain v. Mendez*, 986 F.3d 931 (5th Cir. 2021) ("*Rotstain*") reinforce the conclusion that the *Jinsun* Plaintiffs' claims are derivative of those held by the Receiver. In both *Zacarias* and *Rotstain*, the Fifth Circuit upheld orders barring claims from potential plaintiffs similarly situated to the *Jinsun* Plaintiffs because those plaintiffs' claims were derivative of claims held by a receiver. *Zacarias*, 945 F.3d at 897; *Rotstain*, 986 F.3d at 941.

Like the investors in *Zacarias*, the *Jinsun* Plaintiffs are investors who seek recovery in Texas state court for their "alleged [Breitling]-scheme losses…[under] the Texas Securities Act…and common-law theories of negligence and fraud." *Zacarias*, 945 F.3d at 893-94. And like the investors in *Zacarias*, the *Jinsun* Plaintiffs are pursuing claims against a third-party, Rothstein Kass, for its interactions with receivership entities that they contend furthered the underlying fraudulent scheme that harmed them. *Zacarias*, 945 F.3d at 900-02; *see also* *Rotstain*, 986 F.3d at 941 ("As in *Zacarias*, the Defendants here are alleged to be participants in

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Bering—not BOG or BRC. Thus, separate and apart from the derivative nature of this claim, the *Jinsun* Plaintiffs' theory relating to a violation of the Texas Securities Act is fatally flawed.

the Ponzi scheme, even if unknowing ones, and the investors' claims are based on conduct in furtherance of that scheme."); Dkt. No. 587 at 7-8 ("Rothstein Kass knew there was widespread fraud within Breitling; however, it failed to disclose it. Had Rothstein Kass blown the whistle…State Court Plaintiffs would not have allowed Bering to go forward with the transaction. . . .").

Further, because the *Jinsun* Plaintiffs' claims are *derivative of injuries to Bering*, a Receivership Entity, such claims are derivative of the Receiver's own claims, which seek to recover on behalf of investors in the Receivership Entities like the *Jinsun* Plaintiffs. *Rotstain*, 986 F.3d at 940 (noting that third-party claims in *Zacarias* were derivative where the receiver sought to recover injuries based on additional liabilities incurred to the receivership, and "the [*Jinsun* Plaintiffs'] claims depended on that injury; had the [Receivership Entities] not been injured, neither would the individuals who invested in them."). Finally, the *Jinsun* Plaintiffs' claims compete for Receivership assets and are therefore derivative of the Receiver's claims. *Zacarias,* 945 F.3d at 900 (third-party claims competed for receivership assets because recovery for third-parties was recovery the Receiver could not receive). The *Jinsun* Plaintiffs cannot overcome the Fifth Circuit's holdings in these cases, whether in their Motion or in any objections they may make to the Settlement Agreement or Bar Order.[14]

Reneker v. Offill, No. 3:08-cv-1394, 2009 WL 804134 (N.D. Tex. March 26, 2009)—cited (and mischaracterized) by the *Jinsun* Plaintiffs—does not prove otherwise. (*See* Dkt. No. 587 at 5, 13-15.) Rothstein Kass has never admitted that the *Jinsun* Plaintiffs have standing to

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[14] The *Jinsun* Plaintiffs appear to have previously conceded that the Fifth Circuit's holding in *Zacarias* applies with full force now that the Receiver and Rothstein Kass have reached a settlement. (*See* Dkt. No. 500 at 7 ("*Zacarias* only applies when the Receiver settles with a defendant, like Rothstein Kass. There is no settlement so that case is inapplicable.").)

assert claims against Rothstein Kass. To the contrary, in its summary judgment motion in the *Receiver* Action Rothstein Kass argued that the Receiver does not have standing to assert claims for damages suffered by purchasers of oil and gas interests sold by Breitling.[15] The fact that the Receiver may lack standing to pursue Rothstein Kass for losses incurred by purchasers of oil and gas interests does not logically supporting a conclusion that Bering shareholders have standing to assert claims, or recover damages, that belong to Bering.

Nor does *Sterling Trust v. Adderly*, 168 S.W.3d 835 (Tex. 2005) help the *Jinsun* Plaintiffs' standing argument. (*See* Dkt. No. 587 at 15-16.) Critically, the plaintiffs in *Sterling Trust* appear to have had independent contacts with Sterling Trust Company ("Sterling") (the custodial trustee for many promissory notes used in Avalon Custom Homes' fraudulent scheme) because the plaintiffs provided their retirement money to Sterling. *See Sterling Trust*, 168 S.W.3d at 837-38 ("From 1994 until 1997, Sterling served as the exclusive trustee over the retirement money that the investors self-directed to Cornelius."). In contrast, the *Jinsun* Plaintiffs admit that they never had any independent communications with Rothstein Kass. (App. at 264, Ex. G.) Furthermore, the jury's verdict at the *Sterling* trial included a finding that "Sterling breached its fiduciary duty to its account holders," *Sterling Trust*, 168 S.W.3d at 839, whereas the *Jinsun* Plaintiffs have not pleaded—and cannot plead—that Rothstein Kass separately owed them any duties. (*See, e.g.*, App. at 20-22, Ex. A (alleging only that Breitling's officers and directors owed them fiduciary duties).) Indeed, the fatal issue in the *Jinsun* Plaintiffs' pleading theory—that they seek to recover damages for injuries suffered by a

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[15] Of course, the Receiver opposed this argument in his opposition to Rothstein Kass's summary judgment motion. (*See, e.g.*, *Receiver* Action, Dkt. No. 100 at 59-61.) The Court has not ruled on this argument.

corporation (*i.e.* Bering or BECC)—is wholly absent from *Sterling Trust*, which concerns claims from individual investors who bought securities sold as part of a Ponzi scheme.

IV. CONCLUSION

For the reasons discussed above, Rothstein Kass respectfully requests that this Court deny the Motion and allow the Stay Order to remain in force at least until the Court rules on the pending motions relating to the Settlement Agreement and Bar Order.

Dated: April 28, 2021

Respectfully submitted,

/s/ Nicolas Morgan

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing document has been served on all counsel of record through the Court's electronic filing system on April 28, 2021.

/s/ Nicolas Morgan
Nicolas Morgan